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Central Intelligence Agency



Washington, D.C. 20505

Executive Registry

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11 MAR 1985

Major General William E. Cooper, Jr., USA  
Deputy Director for Foreign Intelligence  
Defense Intelligence Agency  
Washington, D.C. 20301

Bill,

Thank you for your 27 February letter on Soviet defense costing. We share your concern and have recently undertaken steps to reduce some of the confusion in this area.

An Interagency Intelligence Memorandum on Soviet military production was commissioned just last week. It will be managed jointly by the National Intelligence Officers for Strategic Programs and for General Purpose Forces. This paper will provide agreed figures and clearly articulate the nature and source of specific differences between agencies. In doing so, it will result in a common starting point for estimates of procurement expenditures.

Differences in our expenditure estimates will still remain because of significant differences in our cost estimating methodologies. Our past efforts to produce joint expenditure and cost estimates have foundered because our approaches are so different that they cannot be laid out in detailed comparisons. Consequently, as a second step to narrow our differences, the DCI's Military Economic Advisory Panel has been tasked with examining and comparing (where possible) the methodologies. This review began last year and is continuing. The next meeting of the Panel will be in May 1985.

Thanks again for your letter.

Sincerely,

  
John N. McMahon

Deputy Director of Central Intelligence

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**SUBJECT: Letter for Major General William E. Cooper, Jr. USA**

**D/SOVA:DJMacEachin:**  (5 March 1985)

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DDI- 01216/85

6 March 1985

MEMORANDUM FOR: Deputy Director of Central Intelligence

THROUGH: Deputy Director for Intelligence Y

FROM: Douglas J. MacEachin  
Director of Soviet Analysis

SUBJECT: General Cooper's Letter on Soviet Defense Costing Work

1. General Cooper has asked for a comprehensive interagency examination of the methods and estimates related to Soviet defense costs. We can certainly sympathize with his desire to reduce the confusion in this area. We recommend that you respond by laying out a two-phase approach; which in fact is already underway:

- An Interagency Intelligence Assessment on Soviet military production.
- A review by a Panel of experts of the cost estimating methodologies used by the two agencies.

2. An Interagency Intelligence Assessment on Soviet military production was commissioned just last week, to be managed jointly by NIO/SP and NIO/GPF. This paper, by providing agreed figures and by identifying and describing the nature and source of specific differences, will at least result in a common starting point for the estimates of procurement expenditures. In effect, it will constitute a national estimate of the "buy".

3. There will still remain differences in expenditure estimates because of the divergent overall cost estimating methodologies. Our past efforts to produce joint expenditure estimates have foundered because the approaches are so different that they cannot be laid out in detailed comparisons. In fact, DIA's own ruble and dollar estimates have no common base and cannot even be compared to each other. (General Cooper's letter, in our view, reflects a less than complete understanding of this situation. A brief comparison of these differences is laid out in Attachment A.) Consequently, the DCI's Military Economic Advisory Panel has been tasked with examining and comparing the methodologies. The Panel met with and received briefings by DIA officers

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SUBJECT: General Cooper's Letter on Soviet Defense Costing Work

last November, and two members-

[redacted] of Duke University--have been assigned to gather further information and submit a report at the next Panel conference scheduled for May.

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4. Attachment B is a draft letter for you to send to General Cooper, laying out these points.

5. For your information, we are unaware of the basis for General Cooper's statement in paragraph 2, regarding "The difficulty arising from the recent change made by the CIA in the base of the dollar cost calculations...." We suspect it was triggered by the fact that, after refusing earlier requests, we recently released a set of updated cost comparisons after being inundated with DOD demands to do so. This created a messy situation for DIA, who had been answering internal and external requests for these data by rough extrapolation of our last published work (1983).

[redacted]

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Douglas J. MacEachin

Attachments:

Tab A: CIA and DIA Approaches to Estimating  
Soviet Defense Expenditures:

A Brief Comparison

TAB B: Letter to Maj. Gen. William E. Cooper

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Attachment A

CIA and DIA Approaches to Estimating Soviet Defense Expenditures:  
A Brief Comparison

- CIA**
- Both the ruble and dollar estimates are derived from a common detailed description of all categories of Soviet defense spending--procurement, personnel, construction, operations and maintenance, and RDT&E. This common base includes a detailed, building block estimate of all weapons systems and military equipment purchased by the military services.
    - ° The ruble estimate portrays what we estimate that the Soviets actually spent in all categories. It is calculated in constant rubles.
    - ° The dollar estimate portrays what the Soviet military forces would cost the US.

Comment: This is an important but often obscured distinction. The dollar estimate is not simply a conversion of ruble prices to dollars; for both CIA and DIA, the ruble figures are what we believe the Soviets spent, while the dollar figures are what we estimate the US would have spent to buy the same thing.

- DIA**
- The dollar costs are prepared from detailed military production estimates for about one-half of Soviet military procurement. From this, DIA tries to infer what is happening for overall procurement. DIA further extrapolates from this resultant procurement estimate to characterize total defense costs, but does not produce a specific estimate for the total.
  - DIA's ruble figure for total defense spending is derived from the assumption (purported to be based on interpretations of reporting) that defense spending bears a fixed proportional relationship--one third--to the officially published figure for the overall state budget.
  - A ruble figure for procurement outlays is derived by taking the Soviets officially published figure for total value of machinery production and deducting separate estimates of deliveries for non-defense uses. The residual is considered to be for military procurement.

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In sum, while we are acutely conscious of the uncertainties in our own estimates, these estimates at least attempt to be comprehensive in dealing with all categories of defense expenditures, and they are internally consistent in that both the dollar and ruble estimates are based on a common description of the forces and their operational characteristics, and military production.

We believe DIA's dollar estimates are not comprehensive because they attempt to extrapolate from partial estimates. Their estimates are not internally consistent because the ruble and dollar estimates are developed in ways that are totally unrelated to each other. Indeed, their ruble figure for procurement is developed from a process that is not tied to their figures for total defense spending, or to actual observed military material.

Finally, because of the way DIA compiles its ruble estimates, they are necessarily in current rubles; because they are not based on prices they cannot be deflated and consequently they cannot be expressed in constant ruble estimates.

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**CENTRAL INTELLIGENCE AGENCY**

**OFFICE OF THE DEPUTY DIRECTOR**

1 March 1985

NOTE FOR: Associate Deputy Director for Intelligence  
FROM: Executive Assistant to the DDCI

Dick:

Please have someone prepare an appropriate response to this in a day or two. I understand something might already be in the mill.

Thanks,



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**DEFENSE INTELLIGENCE AGENCY**  
WASHINGTON, D.C. 20301

Executive Registry

85- 887

27 FEB 1985

D-0394/DB

Mr. John McMahon  
Deputy Director of Central Intelligence  
Central Intelligence Agency  
Washington, D.C. 20505

Dear John:

1. During the past few months, it has become increasingly clear that both the DIA and the CIA need to address the issue of Soviet defense costs with some degree of accord. While I am not suggesting that either agency cede any independence, it appears that we must be prepared to present as representative and harmonious a picture as possible if we are to be responsive to our many customers in the Executive Branch and Congress. This is particularly the case with the considerable public attention this issue periodically receives.

2. The difficulty arising from the recent change made by the CIA in the base of the dollar cost calculations and subsequent release exemplifies what happens when each agency goes its own way on an issue directly impacting on many major customers.

3. To avoid apparent divisive situations in the future, I strongly recommend that a joint DIA-CIA effort -- the outcome could be an IIA - be undertaken as soon as possible, with an unconditional and unequivocal mandate to accomplish the following with respect to the dollar estimates.

a. Devise an approach to presentations that encompasses the range of honest differences that remain unresolved;

b. Review DIA's and CIA's estimates of production and procurement of Soviet weaponry, to resolve, wherever possible, any differences between the two agencies that have not been settled at the working level. It is not likely that all the differences, some of which are indeed of significant magnitude, can be resolved; where we cannot, then at least we will all have a better understanding of the nature of these differences and the extent to which they impact on the overall estimates.

c. Conduct a "zero-base" review of the concepts, definitions and methodologies underlying the dollar costs. My staff has some serious reservations about the dollar costing methodologies, some of which stems from the fact that much of its framework was established many years ago. Despite the fact that military doctrine has been modified and our understanding and assessments have improved during the past couple of decades, this has gone unrecognized in the process of estimating military outlays. We need to determine what activities should be included or excluded from the estimates (such as leadership protection efforts designed to assure both national entity survival and the capability to prosecute a war; military construction troops).

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4. Our staffs need to examine underlying factors and estimates in order to resolve some significant differences. I have in mind the following examples: the personnel estimates, where we do not have agreed-upon community estimates of manpower levels and we employ U.S. pay rates, yet Soviet soldiers are not paid, trained, or generally as capable as equivalent U.S. troops. The second item pertains to the costs of developing and utilizing the latest technologies in the new weapon systems, and whether the present methodology adequately captures these increased costs. The third item is to examine operating and maintenance factors, with specific attention to those that have changed over the years, particularly with the introduction of newer, more technologically complex weaponry and equipment. Finally, we need to assure ourselves that the estimate of the level and direction of research and development outlays is the best the Community can provide.

5. These items by no means exhaust the list of concerns, but do serve to indicate the breadth of the problem. Many of these points complement and amplify issues raised in the "Blue ribbon" report when members of the MEAP reviewed and critiqued CIA's methodologies for estimating Soviet defense spending for the DCI in 1983. If we in the Intelligence Community are to produce the best possible product and maintain credibility, we must work together closely, and on a continuing basis. I see the advantages of this process as encouraging the reexamination and sharing of information on a wide range of military intelligence issues as well as on military economics. Further, I believe that the results of this effort should be brought before the NFIB in a special session that would lay out its substance and methodological aspects.

6. Finally, you should know that I have urged General Williams and he is attempting to schedule a breakfast with you to discuss the approaches outlined above as a way to help us all deal with the issue in the future.

Sincerely,

←  
Sunday,  
7 March

*Bill*

WILLIAM E. COOPER, JR.  
Major General, U.S. Army  
Deputy Director for Foreign  
Intelligence

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